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No. 81-2391

IN THE

Supreme Court of the United States

October Term, 1982

WESTINGHOUSE ELECTRIC CORPORATION,
Appellant,

against

JAMES H. TULLY, JR., *et al.*, as the Tax Commission of the State of New York,
Appellees.

ON APPEAL FROM THE COURT OF APPEALS OF THE STATE OF NEW YORK

BRIEF OF APPELLEES

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Dated: July 14, 1983

Question Presented.

Whether the New York Tax Law violates the Commerce Clause of the United States Constitution and the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution insofar as it provides for a credit against corporate franchise tax liability of corporate shareholders of domestic international sales corporations (DISCs), where the credit is computed only with respect to the New York income of DISCs attributable to shipments of export property from regular places of business of the corporate shareholders in New York.

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No. 81-2394

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1982

WESTINGHOUSE ELECTRIC CORPORATION,

Appellant,

against

JAMES H. TULLY, Jr., *et al.*, AS THE TAX COMMISSION OF THE STATE OF NEW YORK,

Appellees.

ON APPEAL FROM THE COURT OF APPEALS OF THE STATE OF NEW YORK

BRIEF OF APPELLEES

Decisions Below

The opinion of the Court of Appeals of the State of New York is reported at 55 NY2d 364, 434 NE2d 1044 and 449 NYS2d 677, and is reprinted in the Joint Appendix ("JA") at pages 57-66. The opinion of the Appellate Division, Supreme Court of the State of New York, Third

Judicial Department, is reported at 82 AD2d 988 and 440 NYS2d 397, and is reprinted at JA, pp 50-54. An unpublished order of the Appellate Division, dated June 29, 1981, appears at JA, pp 55-56. The unpublished order of the Supreme Court of the State of New York, Albany County, transferring the proceedings to the Appellate Division, dated January 25, 1980, appears at JA, pp 48-49. The unpublished decision of the New York State Tax Commission, dated August 31, 1979, appears at JA, pp 41-47.

Jurisdictional Basis of Appeal

This is a limited appeal from a judgment of the Court of Appeals of the State of New York which upheld the provision of New York Tax Law, Article 9-A, Franchise Tax on Business Corporations, which imposes a tax on corporations measured by New York allocated entire net income including the income of a DISC of which the taxpayer is a shareholder and provides for some credit against that tax with respect to income from the sale of export property included therein. This Court in noting probable jurisdiction on January 17, 1983, limited it to question 1 presented by the jurisdictional statement as follows:

> "Whether the grant by New York State of a large credit against the franchise tax payable by the corporate parent of a domestic international sales corporation ('DISC') *only* with respect to income attributable to shipments made from New York violates the Commerce Clause of the United States Constitution and the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution?"

Constitutional, Statutory Provisions and New York Tax Regulations

The pertinent text of the constitutional and statutory provisions involved in this case appears in the appendix to this brief as indicated:

Article I, §8, clause 3 (Commerce Clause) of the United States Constitution appears at page A-1.

Amendment XIV, § 1 of the United States Constitution appears at page A-1.

New York Tax Law, Article 9-A, §§ 208.1, 208.8, 208.8-A, 208.9(a), 208.9(i), 209.1, 209.6, 210.1-210.3, 210.13, 211.1 and 211.4 (McKinney 1966 and 1974 Supp), the provisions governing the State franchise tax on DISCs as in effect during the relevant years, appear at pages A-1 - A-13.

New York State Commission Regulations, §§ 5-4.1 - 5-4.3, although not in effect for the years involved, conform to the pertinent provisions of the Tax Law for the relevant years, appear at pages A-14 and A-15.

Statement of the Case

A. Federal and New York taxation of corporations which are shareholders of domestic and international sales corporations.

Under the Internal Revenue Code of 1954, §§ 991-997 (Public Law 92-178) for taxable years beginning after 1971, a domestic sales corporation whose income is predominantly (95%) derived from export sales and rentals may defer paying United States tax up to 50% of that

income. The other half is taxed directly to shareholders even though it is not distributed to the shareholders, but under the law is "deemed" distributed to them. Such distributions are deemed part of such shareholders' Federal taxable income. A corporation entitled to this treatment is referred to as a "Domestic International Sales Corporation" (DISC). The tax-deferred income (accumulated income) is never taxed to the DISC. Such income is taxed to the shareholders only when distributed, when a shareholder sells his stock, or when the corporation no longer qualified as a DISC. The 50% of the DISC's income that is taxed directly to shareholders, certain other constructive distributions, and actual distributions to shareholders are treated as dividends (but, in the case of actual distributions, only to the extent that they exceed income previously taxed directly to shareholders). A DISC may not join in filing a Federal consolidated return. Under the intercompany pricing rules of the Federal law, a DISC may earn profits although in excess of profit it would earn in an arm's length transaction and regardless of the sales price actually charged on products which it purchases from a related company and then resells for export. IRC, § 994.

New York does not tax a DISC, such as Westinghouse Electric Export Corporation, which, during a taxable year, received more than 5% of its gross receipts from the sale or rental of property of its shareholders.

When a corporate taxpayer subject to franchise taxes under Article 9-A of the New York Tax Law is a shareholder of an exempt DISC, the corporate taxpayer must file its own tax report and a consolidated report with the DISC. The consolidated report must contain the attributable share (based on percentage of stock ownership)

of the receipts, expenses, assets and liabilities of the DISC as well as the property, receipts and wages of the DISC eligible for use in the computation of the business allocation percentage. The corporate taxpayer must adjust its receipts, expenses, assets and liabilities to include its attributable share of the DISC's receipts, expenses, assets and liabilities; eliminate any deemed or actual distributions received from the DISC to the extent already included in entire net income; and eliminate intercorporate transactions between the corporate taxpayer and the tax exempt DISC (McKinney's New York Tax Law, §§ 208 [9] [i], 210[3] [a]).

New York State allows a shareholder of exempt DISCs a DISC export credit, computed separately for each DISC, after allowance of various credits such as for an eligible busines facility and the credit for investment in production facilities. The credit is computed by multiplying the shareholder's share of accumulated DISC income by the ratio of gross receipts received from the sale of export property sold by the DISC shipped from a regular place of business of the shareholder in New York over the total gross receipts from the sale of export property sold by the DISC, then multiplying that product by the shareholder's New York business allocation percentage, multiplied by 70%, and multiplied by the shareholder's rate of New York tax (9% in the years under review, 1972 and 1973).

B. Factual Statement.

As stipulated and found by the New York State Tax Commission, the appellant, Westinghouse Electric Corporation (Westinghouse), is a Pennsylvania Corporation which does business in New York. It is engaged in the

manufacture and sale of electric equipment, parts and appliances. Westinghouse owns all the stock of Westinghouse Electric Export Corporation (Westinghouse DISC), a Delaware corporation, which elected to be treated as a domestic international sales corporation for Federal income tax purposes and was so treated for the years 1972 and 1973. It qualified as a DISC under IRC, § 992(a) and was exempt from Federal income tax for such years under IRC, § 991 (JA, p 42).

Westinghouse DISC was a commission agent for Westinghouse and its affiliated companies in respect of export sales of property and related services. All of Westinghouse's DISC's business income for 1972 and 1973 consisted of commissions paid it for such sales for those companies. Westinghouse's DISC had no employees, did not engage in any business activities in New York and did not employ capital, own or lease real or tangible personal property, pay real estate rentals or maintain an office in New York State at any time during such years (JA, pp 42, 43). (It appears that Westinghouse's DISC had no employees of its own and did not own any real or tangible personal property, or pay real estate rentals anywhere [JA, p 9].)

The DISC's sources of income for 1972 and 1973 are as follows (JA, p 43):

Sources of Income	1972	1973
From Westinghouse	$19,888,000	$47,180,132
From affiliated companies of Westinghouse	6,099,000	10,768,606
TOTALS	$25,987,000	$57,948,738

The affiliated companies did not do business in New York State.

Under the provisions of IRC, § 995(b), of these amounts $12,956,500 for 1972 and $29,838,006 for 1973 was deemed distributed to Westinghouse during those years. Westinghouse accordingly included those amounts in its Federal gross income for those years. Federal taxation of the remainder of Westinghouse DISC's income for those years was deferred under the provisions of the Internal Revenue Code (JA, p 43).

Westinghouse DISC made no distribution of income in 1972, but in 1973 it distributed $10,068,500 to Westinghouse. For Federal purposes, this distribution was treated as made out of previously taxed income under IRC, § 996(a) (1) (JA, p 43).

Westinghouse filed New York State corporation franchise tax returns for these years in which it reported entire net income of $136,516,711 for 1972 and $43,715,850 for 1973. These amounts included the $12,956,500 and $29,838,006 deemed distribution of income from Westinghouse DISC for those respective years. The reported income did not include any portion of Westinghouse DISC's accumulated income which was deferred for tax purposes under Federal law.

On the New York State returns, Westinghouse's reported entire net income was allocated to New York State under "business allocation percentages of 6.387743% for 1972 and 6.239516% for 1973 computed without regard to such deemed distributions" by Westinghouse DISC. Westinghouse paid New York State franchise taxes in the amount of $749,384 for 1972 and $205,548 for 1973 (JA, pp 43, 44, 46).

After an audit of Westinghouse, notices of deficiency were issued for the years in the amount of $73,970.23 plus interest for 1972 and $151,436.76 plus interest for 1973. An error was made in the calculation of the deficiency for 1972 because of a transposition of a number. The deficiency of tax, if the error had not been made, should be $71,970 for that year (JA, pp 44, 46).

The notices of deficiency of tax were computed by the New York State Tax Commission on the following basis:

(a) Because more than 5% of Westinghouse DISC's gross receipts in both 1972 and 1973 consisted of sales commissions from Westinghouse, Westinghouse DISC is exempt from New York State franchise tax under section 208(9) (i) (A) of the New York Tax Law, whether or not New York State otherwise had jurisdiction to subject it to tax. Westinghouse is required under section 208(9) (i) (B) of the New York Tax Law to consolidate Westinghouse DISC's receipts, expenses, assets and liabilities with its own in computing its New York State income tax liability, excluding all transactions between Westinghouse and Westinghouse DISC. Since Westinghouse included only the deemed distributions from Westinghouse DISC for 1972 and 1973, and not all Westinghouse DISC's income for such years in its own entire net income for 1972 and 1973, Westinghouse's entire net income for 1972 was increased by $13,390,500 (correct amount should be $13,030,500) from $136,516,711 to $149,907,211 and its entire net income for 1973 was increased by $28,110,732 from $43,715,850 to $71,826,582 (JA, pp 43, 44);

(b) The receipts factors used to compute Westinghouse's business allocation percentages for 1972 and 1973 were recomputed by adding Westinghouse DISC's commission

income derived for such years from customers other than Westinghouse (which other customers did not do business in New York State and were not subject to New York tax) to the denominator of such factors, but not to the numerator, thus reducing Westinghouse's receipts factor for 1972 from 5.945712% as reported on its 1972 return to 5.935845% and reducing its receipts factor for 1973 from 5.665182%, as reported on its 1973 return, to 5.650114%. Such a calculation results in a reduction of Westinghouse's business allocation percentage for 1972 from 6.387743% to 6.384454% and for 1973 from 6.239516% to 6.234494%. The net effect of the two adjustments for 1972 described above increased Westinghouse's business income for 1972 allocable to New York State from $8,683,334 to $9,533,778, an increase of $850,444, with a resulting deficiency in tax for 1972 of $76,539.96. Similarly, the net effect of the adjustments for 1973 described above increased Westinghouse's business income for 1973 allocable to New York State from $2,702,912 to $4,453,304, an increase of $1,750,392, with a resulting deficiency in tax for 1973 of $157,535.28 (JA, pp 44, 45);

(c) Westinghouse was allowed credits under section 210(13) (a) of the Tax Law in the respective amounts of $2,569.77 and $6,098.22 for 1972 and 1973. Such credits were computed by first multiplying $13,390,500 and $28,110,732, representing accumulated Westinghouse DISC income for 1972 and 1973 respectively, as computed by the auditor, by 4.771297% and 5.523182%, respectively. Those percentages are the percentages of Westinghouse's receipts from export property on which Westinghouse DISC earned a sales commission and which were shipped from a regular place of business of Westinghouse in New York as compared to Westinghouse's total receipts on the sale of export property for such years for which

Westinghouse DISC received a sales commission. Such total receipts amounted to $223,587,000 in 1972 and $408,080,000 in 1973 (JA, pp 45, 46).

The respective products, $638,091 for 1972 and $1,552,607 for 1973, were then multiplied by Westinghouse's revised business allocation percentages for the respective years, with the result that of the $13,390,500 and $28,110,732 includable in Westinghouse's entire net income for 1972 and 1973, respectively, only $40,790 and $96,797 respectively, were found to be eligible for credit under section 210(13) (a). These amounts were then multiplied first by 70% and then by the 9% rate of tax in effect for 1972 and 1973 to arrive at credits of $2,569.77 and $6,098.22 for 1972 and 1973, respectively (JA, p 46).

C. Proceedings Below.

Westinghouse filed a petition for a redetermination of the notices of deficiency issued for 1972 and 1973. In the petition it contended that by requiring Westinghouse to compute its franchise tax liability by combining its receipts and expenses with those of Westinghouse DISC, thereby taxing accumulated DISC income and deemed distributed income of Westinghouse DISC, appellees violated the Commerce Clause of the United States Constitution and the Due Process and Equal Protection Clauses of the Fourteenth Amendment. Westinghouse also contended that limiting the export credit to income attributable to shipments made from a regular place of business in New York State violated the Commerce Clause and the Equal Protection Clause. The State Tax Commission's determination denied Westinghouse's petition (JA, pp 41-47).

Westinghouse brought a proceeding in the New York Supreme Court for judicial review of the State Tax Commission's determination in which it again raised its constitutional claims. The proceeding was transferred to the Appellate Division, Third Department, for disposition (JA, pp 48, 49).

The Appellate Division, two Justices dissenting, held that New York Tax Law, § 208(9) (i) (B), to the extent it requires Westinghouse DISC's accumulated income be added to Westinghouse's income, is unconstitutional on the ground that it settles an impermissible burden on foreign commerce (JA, pp 50-54).

The State Tax Commission appealed from that portion of the Appellate Division's decision that invalidated section 208(9) (i) (B), and Westinghouse cross-appealed to the extent that the Appellate Division had upheld the tax on deemed distributions. Westinghouse raised the consitutional claims that it had presented before the State Tax Commission and the Appellate Division, and which it claims before this Court. The Court of Appeals rejected Westinghouse's constitutional claims and upheld the franchise tax in all respects (JA, pp 57-66). Its order modified the order of the Appellate Division and reinstated the determination of the State Tax Commission (JA, p 67).

The New York Court of Appeals, in discussing the export tax credit, said:

> "Here the record shows that Westinghouse and its DISC were operating a unitary business. Not all the accumulated DISC income was subjected to taxation, but rather only that part allocable to New York (Tax Law, §§ 208.9[i] [B], 210.1[a], 210.3; *cf.*

Fischbach & Moore v. Tax Comm., 36 N.Y.2d 605, 607). Moreover, there is nothing in the record to show that the income was improperly apportioned to business done in New York; nor does the taxpayer question our State's allocation formula.

* * *

"[Westinghouse] reasons that the effect of the credit is impermissibly to subject its export sales from a non-New York 'place of business' to a higher rate of tax than comparable sales 'shipped from a regular place of business' within New York.

* * *

"The first step to be taken to arrive at the amount of such tax credit is to multiply the taxpayer's share of the accumulated DISC income by the taxpayer's New York 'business allocation percentage' (Tax Law, § 210.3). This yields the dollar value of the accumulated DISC income allocable to New York as *instate* earnings. This amount is then multiplied by that percentage which the taxpayer's receipts from export property on which the DISC earned commissions *and* which was shipped from a regular place of business in New York bears to the taxpayer's total receipts from the sale of export property on which the DISC earned commissions. The product of this calculation is the amount eligible for the credit; it is merely a subdivision of the accumulated DISC income allocable to New York.

"Obviously, the business allocation percentage plays an integral role in computing the tax credit. It

determines what amount of the taxpayer's income has a jurisdictional nexus with the State. The result is that, when the State exercises its taxing power, it does so consistently with due process mandates [citations omitted].

"But New York need not tax all which it has the right to tax. The credit here simply forgives a portion of that income which New York may tax by reference to shipments of export property from a regular place of business in New York, an additional New York relationship. Such a method clearly satisfies due process, and any effect on interstate commerce is too indirect to run afoul of the commerce clause." (JA pp 63-65).

Summary of Argument

Contrary to the assertions of Westinghoue, New York taxes only income reasonably allocated to it. In order to subject New York DISC income to New York franchise taxes, New York requires that the corporate shareholder consolidate its income with its share of DISC income. An allocation of all that income is then made to New York. The New York franchise tax is imposed on the corporate shareholder solely on the income allocated to New York.

A tax credit, which is now the only subject of this appeal, is allowed against this tax. A credit is determined based upon the percentage of receipts which is derived from the shipment of export property from a regular place of business of the taxpayer in New York. The effect of the credit does not place a higher tax on the taxpayer on its export sales from a non-New York place of business but merely lessens the tax on its New York income resulting from shipments of export property from a New York regular place of business of the taxpayer. Such income is

taxed because it is earned in this State. Income from non-New York business is not taxed by New York and accordingly no credit is given for business income which is not derived from New York sources.

The credit is given to enable New York to compete with other States. States are free to use their taxing power "to encourage the growth and development of intrastate commerce and industry * * * [and to] compete with other States for a share of interstate commerce; such competition lies at the heart of a free trade policy" (*Boston Stock Exchange v. State Tax Comm.*, 429 US 318, 336-337 [1977]). That this is what the credit allowed by section 210.13(a) accomplishes, and no more, is demonstrated by an analysis of how it is calculated. Experience demonstrates that the export tax credit has not resulted in an increase in New York's export business. Its percentage of such business has been declining since 1972. There is no way to demonstrate by the record that New York's export business has been affected by the credit.

ARGUMENT

The tax credit against New York franchise taxes does not discriminate against or burden interstate commerce in reducing New York taxes on income allocated to New York by limiting the computation of the credit to shipments of export property from a regular place of business of corporate shareholders in New York.

Westinghouse contends (Br, p 21) that New York imposes franchise taxes on the income of a corporate shareholder of a tax exempt DISC which derives from sales shipped from facilities outside of New York and sales of affiliates of the corporate shareholder which affiliates do

not transact business in New York. These claims are wrong factually. New York only taxes income reasonably allocated to New York. Coupled with these falsely premised contentions, appellant argues (Br, p 23) that the New York tax credit, which is limited in its application to shipments from facilities in New York, violates the Commerce Clause of the United States Constitution and the Due Process and Equal Protection Clauses of the Fourteenth Amendment to the United States Constitution. This argument has no substance.

Westinghouse premises its argument on its assertions (Br, p 4) that New York imposes its franchise tax on the income of a DISC (deemed distributions, actual distributions, and accumulated income) "with respect to sales having no relation to New York by *including* in its computation of the DISC's income revenues derived from sales of affiliates not doing business in New York, while *excluding* the receipts, property and payroll of those affiliates from its apportioned calculations". These claims are contrary to fact and are not supported by the record. The only DISC income subject to New York tax is that part allocable to New York. (See opinion of the Court of Appeals below [JA, p 63].) Indeed, in making these assertions, appellant attempts to present issues included in question 2 of its jurisdictional statement which this Court refused to entertain. Question 1 of the jurisdictional statement, the only question before this Court, makes no reference to a Due Process issue. Additionally, Westinghouse has misstated (Br, p 17) the limitation placed on the application of the tax credit in alleging that export shipments are only required to be made from New York. The tax credit is limited to shipments of export property from a regular place of business in New York of the corporate shareholder.

It is undisputed that Westinghouse and Westinghouse DISC are engaged in a unitary business. This fact is no longer in issue in this case in view of this Court's refusal to consider Question 2. Thus, it is appropriate to require the two corporations to file a consolidated New York franchise tax return. However, in view of appellant's fundamental misstatements, a brief summary seems desirable to point out that New York is taxing only New York income. The DISC is a wholly owned subsidiary of Westinghouse and approximately 80% of the DISC income is derived from commissions received from Westinghouse. Westinghouse DISC apparently had no employees of its own and did not own any real or tangible personal property or pay real estate rentals anywhere. In this context, combining Westinghouse and Westinghouse DISC income prior to apportionment, is fully justified. See *Container Corporation of America v. Franchise Tax Board*, ____ US ____ (1983); *Mobil Oil v. Commissioner of Taxes*, 445 US 425 (1980); *Exxon Corp. v. Wisconsin Department of Revenue*, 447 US 207 (1980); *F. W. Woolworth v. Taxation and Revenue Dept*, 458 US ____ (1982); *Asarco, Inc. v. Idaho State Tax Commission*, 458 US ____ (1982).

Indeed, New York has long required or permitted affiliated companies to file franchise tax returns in which their income is combined where they have substantial intercompany transactions. See *Wurlitzer v. State Tax Commission*, 35 NY2d 100 (1974), 316 NE2d 301, 358 NYS2d 1.

As this Court has recognized, Westinghouse simply failed to demonstrate that the New York Tax Law, by requiring Westinghouse and its DISC to consolidate their income, reaches DISC income derived from affiliates of

Westinghouse which do not do business in New York and which are not engaged in a unitary business with Westinghouse. The entire consolidated net income of Westinghouse and Westinghouse DISC is allocated to New York, by the use of a three-factor formula using the factors of property, wages and receipts within and without New York weighted equally to arrive at a business allocation percentage. This percentage is applied to a taxpayer's entire consolidated net income to arrive at a base on which the tax rate (9%) is applied prior to the application of the tax credit. (The formula's provisons are set out in New York Tax Law, § 210[3].)

Thus, not all of the DISC income is subject to New York taxation. Only the New York portion of the entire consolidated net income of Westinghouse and Westinghouse DISC is taxed.

It is settled that the "entire net income of a corporation, generated by interstate as well as intrastate activities, may be fairly apportioned among the States for tax purposes by formulas utilizing in-state aspects of interstate affairs." *Northwestern States Portland Cement Co. v. Minnesota*, 358 US 450, 460 (1959); *General Motors Corp. v. Washington*, 377 US 436 (1964); *Complete Auto Transit v. Brady*, 430 US 274 (1977); *Mobil Oil Corp. v. Commissioner of Taxes*, 445 US 425, 436-442 (1980). In determining what constitutes "fairly apportioned", this Court has enunciated the following standard:

> 'That the apportionment may not result in mathematical exactitude is certainly not a constitutional defect. Rough approximation rather than precision is, as a practical matter, the norm in any such tax system." *Illinois Central Railroad Co. v.*

State of Minnesota, 309 US 157, 161 (1940), reh den, 309 US 695 (1940).

Westinghouse has not claimed that the application of the New York three-factor allocation formula to its income results in New York taxing income which the State does not have jurisdiction to tax. Indeed, if it had demonstrated in the proceedings below that income of Westinghouse was being improperly allocated to New York by the formula, the New York State Tax Commission could have exercised its authority under New York Tax Law, § 211(5) to adjust the formula so as to equitably determine its New York tax. Aside from being foreclosed by this Court's order in taking jurisdiction of this appeal, Westinghouse's failure to demonstrate that the New York allocation formula reaches income which does not have a nexus in New York forecloses it from now claiming that New York taxes such income.

Much of the appellant's brief is based on the absurd premise that the three-factor formula applied to apportion the income of the corporations in the unitary business (i.e., Westinghouse and Westinghouse DISC) must include the receipts, payroll and property of the customers of the DISC which are not components of the unitary business. Clearly, neither the principles of fair apportionment announced by this Court (nor any statement or holding by this Court) provide any support for this totally erroneous argument concerning apportionment. The instant case is one where fair apportionment is clearly shown because the receipts, payroll and property of Westinghouse and the receipts of Westinghouse DISC are the basis for the three-factor formula apportionment which is applied to the consolidated income of Westinghouse and Westinghouse DISC. As we have already indicated earlier in this brief,

Westinghouse DISC apparently had no employees of its own, did not own real property or tangible personal property or lease real property from others (JA, p 9).

The credit is allowed against the New York tax which is measured by New York income, but only to the extent the commission income also has a New York connection. The burden to show discrimination against interstate commerce rests on the party challenging the statute. *Hughes v. Oklahoma,* 431 US 322, 336 (1979). Contrary to appellant's position, there is no conceivable basis why New York should give a credit for commission (DISC) income that it never taxed in the first instance. As such the tax credit does not discriminate against interstate commerce. The tax and the credit do not affect interstate commerce in any greater degree than any other state tax or credit on business income.

States are not prevented from structuring their tax systems to encourage growth, industry, and interstate commerce. States may compete with other States for a share of interstate commerce although they may not discriminatorily tax products manufactured or the business operations performed in any other State. See, *Boston Stock Exchange v. State Tax Commission,* 429 US 318, 336-337 (1977). It has not been suggested by this Court that States cannot structure their tax systems to compete with other States for a share of foreign commerce. Indeed, such competition between States promotes the Federal goal of increasing exports. States, moreover, have the power to impose a heavier tax burden on one class of taxpayers or income within their borders than on another provided all persons and property in the same class are treated alike. It is well established, of course, that States have broad discretion on classifying corporations

for tax purposes and impose varying taxes on separate classifications. See, e.g., *Walters v. City of St. Louis*, 347 US 231, 237-238 (1954); *Ohio River & W. R. Co. v. Ditty*, 232 US 576 (1914); *People ex rel. Hatch v. Reardon*, 184 NY 431 (1906), affd 204 US 152 (1907); *Metropolitan Street R. Co. v. New York State Board of Tax Comrs.*, 199 US 1 (1904); *Pacific Exp. Co. v. Seibert*, 142 US 339 (1892).

Appellant's reliance (Br, pp 16-17) on *Boston Stock Exchange* is totally misplaced. There, in taxing the sale of securities that would be delivered or transferred in New York, a higher rate of tax applied if the securities were sold by a non-resident through an out-of-state exchange. Moreover, if New York's residents made a large block transaction on a New York exchange, the tax was substantially less than if made through an out-of-state exchange. These extra tax burdens imposed for using out-of-stock exchanges were held to fall short of the substantially evenhanded treatment demanded by the Commerce Clause. But this Court also stated (429 US at 337) that we "hold only that in the process of competition no State may discriminatorily tax the products manufactured or the business operations performed in any other State". Here, of course, New York has taken care not to tax out-of-state income and has simply chosen to tax that part of the taxpayer's New York income stemming from exports (New York related exports since only New York income is being taxed) at a lesser rate than non-export New York income.

Appellant's reliance (Br, pp 16-12) on *Maryland v. Louisiana*, 451 US 725, 754 (1981), is also misplaced. There Louisiana imposed a so-called first use tax on natural gas from the outer-continental shelf, which concededly was to be passed on to consumers of that gas in

much of the country. However, by use of a number of credits and exemptions, Lousiana consumers of gas were to be largely immune from the tax. This tax was also struck down for not treating interstate commerce in an evenhanded manner with intrastate commerce. The case has no relation to the situation here where only income properly allocated to New York is being taxed at all and hence entitled to a credit.

We recognize, of course, that this Court has viewed with suspicion state statutes requiring business operations to be performed in the home State that could be more efficiently performed elsewhere. See *Pike v. Bruce Church, Inc.*, 397 US 137, 145 (1970), which involved a statute which prevented the interstate bulk shipment of cantaloupes grown in Arizona. The statute had the effect of compelling the producer to build unneeded packing facilities in Arizona. This Court held the Commerce Clause does not permit a State to require work to be done within its jurisdiction to enhance the reputation of other producers within its borders.

The New York tax credit does not require business operations to be performed in New York nor does it provide a significant inducement to corporations to conduct export business from a place of business in New York. The small inducement which the credit provides in reality has the same effect as taxing New York income from export business at a lower rate than the same business activities would be taxed if they were not conducted for export. In other words, the tax credit results in a lower effective tax rate. This right of New York to structure its tax scheme to encourage commerce was explicitly recognized in *Boston Stock Exchange, supra*. If the credit is viewed as an indirect subsidy to export commerce, it does not discriminate against interstate commerce. All States give indirect subsidies to commerce in financing facilities such as

ports, airports, waterways and highways, providing job incentive and investment tax credits as well as providing police and fire protection.

Moreover, while we belive a tax credit to encourage local business is appropriate, the Court should recognize that the actual application of the provision here is resulting in very slight credit. (We observe that appellant's underlying position that DISC income should not be taxed at all would result in a larger benefit.)

A "state tax must be assessed in light of its actual effect considered in conjunction with other provisions of the State's tax scheme". *Maryland v. Lousiana,* 451 US 725, 756 (1981); *Complete Auto Transit v. Brady,* 430 US 274 (1977). The practical operation of the tax credit does not discriminate against interstate commerce.

Under Federal law, corporations which are shareholders of DISCs are taxed differently from corporations which are shareholders of corporations which are not DISCs. DISCs are not taxpayers. Shareholders of DISCs are taxed on DISC income for a year in which it is earned or for a year to which DISC income is deferred. Transactions between shareholders of a DISC and a DISC are not limited to arms-length pricing but are permitted to use special pricing arrangements. IRC, §994. The special pricing rules permit the transfer of income from a shareholder corporation to its non-taxed DISCs.

This Federal tax scheme would result in New York income of both the corporate shareholder and its DISC escaping New York franchise taxes unless special provisions were made for their taxation. The New York law prevents New York income of a parent and its DISC from

escaping New York taxes by requiring the corporate shareholders of a tax exempt DISC (taxpayer) and its DISC to consolidate their income. The tax credit does not, as we have seen, result in a benefit being given local business at the expense of out-of-state commerce.

The DISC tax credit is determined separately for each DISC, after allowance of any other credit given for an eligible business facility, certain compensatory use taxes, investment, and employment incentives. If these credits reduce a DISC shareholder's tax below a minimum tax ($125 for the years 1972 and 1973), the tax credit would not be available. New York Tax Law, § 210(13)(a).

The tax credit is computed by multiplying the DISC shareholder's share of DISC accumulated income by the percentage of the gross receipts from sales made by the DISC of export property of the taxpayer (Westinghouse) shipped from the regular place of business of taxpayer within New York by or to the DISC divided by the total receipts from the sale of export property made by or to the DISC. The product is then multiplied by the taxpayer's New York business allocation percentage. The resulting product is then multiplied by 70%, the product of which is then multiplied by the taxpayer's tax rate. The result is the amount of the export tax credit. (New York Tax Law, § 210[13][a]).

Accumulated income is defined by Internal Revenue Code § 996 and in general means total income less actual and deemed distributions. Accumulated income cannot exceed 50% of DISC income.

Under the New York law, "export property" for purpose of the credit is defined by IRC, § 993, subd (c).* To qualify for the credit, the export property must be shipped from "a regular place of business" of the taxpayer within the State. A regular place of business is defined as "any bona fide office (other than a statutory office), factory, warehouse or other space which is regularly used by the taxpayer in carrying on its business". The term "regular place of business" is not defined by the New York Tax Law. It is defined by the Rules and Regulations of the New York State Tax Commission. (See *Matter of Clairmont Mills, Inc. v. New York State Tax Commission,* 11 AD 2d 368, 369 [3d Dept, 1960], 206 NYS2d 621, 622.) The definition which predates the enactment of the New York tax DISC legislation has been incorporated in the New York regulations for purposes of New York tax credit, although the regulations were not promulgated until after the years under review (State Tax Commission Reg, § 5-4.1 [20 NYCRR 5-4.1]). Under the requirements of the formula for computating the export tax credit, the mere shipment of export property from a New York facility is insufficient to qualify for the export tax credit nor do such shipments need to be made from a New York port in order to qualify for the credit.

In 1972, 4.771297% of the receipts from all sales of Westinghouse export property made by Westinghouse DISC were derived from sales in which the export property was shipped from a regular place of business of Westinghouse in New York. However, only .213235% of

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*Export property in general means property manufactured, produced, grown or extracted in the United States by a person other than a DISC, held primarily for sale, lease or rental, in the ordinary course of business by a DISC for disposition outside the United States and not more than 50% of the fair market value of which is attributable to articles imported into the United States.

the accumulated commission income of Westinghouse DISC was and could be deducted under the tax credit formula from the New York allocated and consolidated income of Westinghouse on which the New York franchise tax rate is applied. Similar results also pertain for 1973.

The computation of the DISC export credit allowed Westinghouse for 1972 is shown as follows:

DISC accumulated income		$13,390,500
Percentage of receipts of taxpayer's export property shipped from a place of business of Westinghouse in New York over all receipts from DISC's export sales	X	4.771297%
		638,900.52
Westinghouse's New York business allocation percentage	X	6.384454%
		40,790.31
Statutory reduction percentage	X	70%
		28,553.22
Tax rate	X	9%
Export tax credit		2,569.79

To enable a corporate shareholder of a DISC to make shipments of export property from a regular place of its business in New York, it is necessary for that corporation to have facilities and a staff in New York for that purpose. In providing such New York facilities and staff for shipments from a New York place of business the corporation's New York business allocation percentage would be increased because of higher New York property and payroll factors. Assuming the same total corporate income, its New York franchise tax would be higher, a result that would only be partially offset by the export tax credit.

The example given by Westinghouse to illustrate the application of the tax credit on page 17 of its brief distorts the effect of the credit. As discussed above, the business allocation percentage removes non-New York income from the base on which the New York tax is imposed. When shipments are made from a regular place of business of the taxpayer in New York, the New York business allocation increases as well as the New York tax base. These facts are ignored by Westinghouse.

New York taxes are among the highest in the nation. If other taxes which a corporation must pay to enable it to do business in New York can be considered, the alleged inducement of the tax credit to make shipments from a place of business in New York State becomes more unrealistic. The purpose of giving the tax credit is to prevent export business being driven out of New York and into States which follow the liberal tax treatment given DISC income by the Federal DISC legislation or which impose lower tax rates on such income than the rate being imposed on it by New York. The credit is designed to maintain export business in New York, principally manufacturing, by lowering the tax on such New York business. The tax credit merely lessens the New York tax computed on New York DISC income. If export business in New York decreased or was driven out of the State, the State would suffer a greater tax loss than that caused by the tax credit, as found by the New York Legislature. (See New York Legislative Annual, 1972, p 269).

Experience shows that since 1972 when the New York tax and credit provisions relating to DISCs were enacted, the percentage of United States exports from New York decreased. New York's share in 1972 was 7.6% and in 1980 it dropped to 5.9% as shown by the following table:

EXPORTS OF MANUFACTURED PRODUCTS UNITED STATES, NEW YORK AND OTHER SELECTED STATES*

	(millions of dollars)				Percent Change	
	1960	1972	1976	1980	1960-72	1972-80
United States	14,546	36,608	83,098	155,103	+151.7	+323.7
New York	1,211	2,795	5,320	9,168	+130.8	+228.0
Massachusetts	386	920	2,503	4,719	+138.3	+412.9
New Jersey	783	1,328	2,660	4,409	+ 69.6	+232.0
Pennsylvania	1,083	2,351	4,706	7,580	+117.1	+222.4

	Percent of United States			
	1960	1972	1976	1980
New York	8.3	7.6	6.4	5.9
Massachusetts	2.7	2.5	3.0	3.0
New Jersey	5.4	3.6	3.2	2.8
Pennsylvania	7.4	6.4	5.7	4.9

There is no basis to the claim that New York's scheme of DISC taxation diverts employment and business to New York State which might otherwise go to, and more efficiently be done in, some other State. The tax credit is in effect and in substance no different than a tax credit given for investments in New York which operate to lessen the New York tax on New York income aimed to encourage New York investments. The New York tax is limited to New York income. The tax credit is allowed against New York tax measured by income which is derived from and connected only with New York sources and as such does not discriminate against interstate commerce. It merely reduces New York taxes on New York export businesses.

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*Prepared in the New York State Department of Commerce, Division of Economic Research and Statistics. *Source:* U.S. Bureau of the Census, *Origin of Exports of Manufactured Products.*

CONCLUSION.

The judgment of the Court of Appeals of the State of New York should be affirmed.

Dated: Albany, New York
July 14, 1983

Respectfully submitted,

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CONSTITUTIONAL AND STATUTORY PROVISIONS AND REGULATIONS OF THE NEW YORK STATE TAX COMMISSION INVOLVED

United States Constitution

Article I, Section 8

The Congress shall have Power . . .

[3] To regulate Commerce with foreign Nations, and among the several States and with the Indian Tribes.

Amendment 14, Section 1

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the States wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States, nor shall any State deprive any person of life, liberty or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

New York Tax Law, Article 9-A

(as in effect in 1972 and 1973)

New York Tax Law § 208.

As used in this Article:

1. The term "corporation" includes a joint-stock company or association and any business conducted by a trustee or trustees wherein interest or ownership is evidenced by certificate or other written instrument; a "DISC" and a "former DISC" mean any corporation which meets the requirements of subsection (a) of section nine hundred ninety-two of the internal revenue code of nineteen hundred fifty-four. . . .

New York Tax Law §§ 208(8), 208(8-A)

8. The term "business income" means entire net income minus investment income;

8-A. Provided, however, that with respect to a DISC or a former DISC, the following provisions shall apply:

(a) investments in the stocks, bonds or other securities of a DISC or any indebtedness from a DISC shall not be treated as either subsidiary capital or investment capital under subdivisions four or five of this section,

(b) any amounts deemed distributed from a DISC or a former DISC which are taxable as dividends pursuant to subsection (b) of section nine hundred ninety-five of the internal revenue code of nineteen hundred fifty-four shall be treated as business income, except any such amounts from a former DISC attributable to amounts includible in a taxpayer's entire net income for a prior taxable year under subparagraph (B) of paragraph (i) of subdivision nine of this section shall be excluded from entire net income,

(c) any gain recognized for federal income tax purposes on the disposition of stock in a DISC, and any gain recognized on the disposition of stock in a former DISC, includible in gross income as a dividend pursuant to subsection (c) of section nine hundred ninety-five of the internal revenue code of nineteen hundred fifty-four, shall be treated as business income, and

(d) except as provided in paragraph (i) of subdivision nine of this section, any actual distribution from a DISC or a former DISC shall be treated as business income except an actual distribution which for federal income tax purposes is treated as made out of "other earnings and profits" under section nine hundred ninety-six of the internal revenue code of nineteen hundred fifty-four, in which case such actual distribution shall be treated as either subsidiary income or investment income under this article.

New York Tax Law § 208(9)(a)(1)

9. The term "entire net income" means total net income from all sources, which shall be presumably the same as the entire taxable income which the taxpayer is required to report to the United States Treasury Department, or which the taxpayer would have been required to report, if it had not made an election under subchapter s of chapter one of the internal revenue code, except as hereinafter provided, and subject to any modification required by paragraph (d) of subdivision three of section two hundred ten of this article.

(a) entire net income shall not include:

(1) income, gains and losses from subsidiary capital which do not include the amount of a recovery in respect of any war loss except for such amounts from a former DISC which are treated as business income under subdivision eight-A of this section . . . .

New York Tax Law § 208(9)(i)

(i) With respect to a DISC which during any taxable year or reporting year (1) received more than five percent of its gross sales from the sale of inventory or other property which it purchased from its stockholders, (2) received more than five percent of its gross rentals from the rental of property which it purchased or rented from its stockholders or (3) received more than five percent of its total receipts other than sales and rentals from its stockholders, the following provisions shall apply.

(A) For any taxable year in which sub-paragraph (B) of this paragraph is in effect and not rendered invalid, a DISC meeting the above test shall be exempt from all taxes imposed by this article.

(B) Supplemental to the provisions of subdivision five of section two hundred eleven of this article, any taxpayer required to compute a tax under this article, which during the taxable year being reported was a stockholder in any

DISC meeting the test prescribed in this paragraph, shall for any taxable year ending after December thirty-first, nineteen hundred seventy-one adjust each item of its receipts, expenses, assets and liabilities, as otherwise computed under this article, by adding thereto its attributable share of each such DISC's receipts, expenses, assets and liabilities as reportable by each such DISC to the United States Treasury Department for its annual reporting period ending during the current taxable year of such taxpayer; provided, however, (1) that all transactions between the taxpayer and each such DISC shall be eliminated from the taxpayer's adjusted receipts, expenses, assets and liabilities; (2) that the taxpayer's entire net income as otherwise computed under this section, shall be reduced by subtracting the amount of the deemed distribution of current income, if any, from each such DISC already included in the entire net income of such taxpayer by virtue of having been included in its entire taxable income for that taxable year as reported to the United States Treasury Department; and (3) that in the event this paragraph should be rendered invalid, all DISCs and their stockholders taxable hereunder shall be taxed instead under the remaining portions of this article.

New York Tax Law § 209 (1)

1. For the privilege of exercising its franchise or doing business in this state in a corporate or organized capacity for all or any part of each of its fiscal or calendar years . . . every domestic or foreign corporation, except corporations specified in subdivision four of this section, shall annually pay a franchise tax, upon the basis of its entire net income, or upon such other basis as may be applicable as hereinafter provided, . . . and [the tax] shall be paid as hereinafter provided.

New York Tax Law § 209 (6)

6. For any taxable year of a DISC, not exempt from tax under paragraph (i) of subdivision nine of section two hundred eight of this article, the taxes imposed by subdivision one of this

section shall be computed only under either clause two or clause four of paragraph (a) of subdivision one of section two hundred ten of this chapter, whichever is greater, and paragraph (b) of such subdivision.

New York Tax Law §§ 210(1)-210(3)

1. The tax imposed by subdivision one of section two hundred nine of this chapter shall be, in the case of each taxpayer:

(a) a tax (1) computed at the rate of nine per centum on its entire net income, or the portion thereof allocated within the state as hereinafter provided, subject to any modification required by paragraph (d) of subdivision three of this section, or (2) computed at one and six tenths mills for each dollar of its total business and investment capital, or the portion thereof allocated within the state as hereinafter provided, except that in the case of a cooperative housing corporation as defined in the internal revenue code or in the case of a housing company organized and operating pursuant to the provisions of article two of the private housing finance law, the applicable rate shall be four-tenths of a mill, or (3) computed at the rate of nine per centum on thirty per centum of the taxpayer's entire net income plus salaries and other compensation paid to the taxpayer's elected or appointed officers and to every stockholder owning in excess of five per centum of its issued capital stock minus fifteen thousand dollars (except as hereinafter provided) and any net loss for the reported year, or on the portion of such sum allocated within the state as hereinafter provided for the allocation of entire net income, subject to any modification required by paragraph (d) of subdivision three of this section, or (4) one hundred dollars, whichever is greatest, plus

(b) a tax computed at the rate of eight-tenths of a mill for each dollar of the portion of its subsidiary capital allocated within the state as hereinafter provided.

(c) In the case of a taxpayer which is not subject to tax for an entire year the exemption allowed in clause three

of paragraph (a) of this subdivision shall be prorated according to the period such taxpayer was subject to tax.

(d) If the taxable period for which the tax is due is less than an entire year, the minimum tax fixed by clause four of paragraph (a) of this subdivision shall be reduced by twenty-five per centum if the period for which such taxpayer is subject to tax is more than six months but not more than nine months and by fifty per centum if the period for which such taxpayer is subject to tax is not more than six months.

1-a. Notwithstanding any other provision of this chapter, an additional tax computed at the rate of five and three-quarters per centum on business income, or the portion thereof allocated within the state as hereinafter provided, is hereby imposed on every corporation subject to the tax imposed by this article which has gross receipts of five hundred thousand dollars or more for the taxable year from transportation, within this state, by omnibuses having a seating capacity of more than seven persons, other than receipts for the operation of school buses which are excluded from entire net income.

1-b. The computation specified in clause three of paragraph (a) of subdivision one shall not apply to a corporation organized under article fifteen of the business corporation law.

2. The amount of subsidiary capital, investment capital and business capital shall each be determined by taking the average fair market value of the gross assets included therein (less, in the case of business capital, average liabilities deductible therefrom which are payable by their terms on demand or within one year from the date incurred, other than loans or advances outstanding for more than a year as of any date during the year covered by the report, and, if the period covered by the report is other than a period of twelve calendar months, by multiplying such value by the number of calendar months or major parts thereof included in such period, and dividing the product thus obtained by twelve[)].

3. The portion of the entire net income of a taxpayer to be allocated within the state shall be determined as follows:

(a) multiply its business income by a business allocation percentage to be determined by

(1) ascertaining the percentage which the average value of the taxpayer's real and tangible personal property within the state during the period covered by its report bears to the average value of all the taxpayer's real and tangible personal property wherever situated during such period;

(2) ascertaining the percentage which the receipts of the taxpayer, computed on the cash or accrual basis according to the method of accounting used in the computation of its entire net income, arising during such period from

(A) sales of its tangible personal property where shipments are made to points within this state,

(B) services performed within the state,

(C) rentals from property situated, and royalties from the use of patents or copyrights, within the state, and

(D) all other business receipts earned within the state, bear to the total amount of the taxpayer's receipts, similarly computed, arising during such period from all sales of its tangible personal property, services, rentals, royalties and all other business transactions, whether within or without the state;

(3) ascertaining the percentage of the total wages, salaries and other personal service compensation, similarly computed, during such period of employees within the state, except general executive officers, to the total wages, salaries and other personal service compensation, similarly computed, during such period of all the taxpayer's employees within and without the state, except general executive officers; and

(4) adding together the percentages so determined and dividing the result by the number of percentages; provided, however, that if the taxpayer does not have a regular place of business outside the state other than a statutory office, the business allocation percentage shall be one hundred percent;

Provided, however, that any taxpayer required to adjust its receipts, expenses, assets and liabilities by adding an attributable portion of the receipts, expenses, assets and liabilities of any DISC, as provided by paragraph (i) of subdivision nine of section two hundred eight of this article, shall substitute such adjusted figures in computing the percentages required in subparagraphs one, two and three of this paragraph.

(b) multiplying its investment income by an investment allocation percentage to be determined by

(1) multiplying the amount of its investment capital invested in each stock, bond or other security (other than governmental securities) during the period covered by its report by the percentage, if any, of the entire capital or the issued capital stock, or the gross direct premiums, or the net income, as the case may be, of the issuer or obligor thereof required to be allocated within the state on the report or reports, if any, required of any such issuer or obligor under this chapter or the insurance law for the preceding year, but without regard to any minimum,

(2) adding together the sums so obtained, and

(3) dividing the result so obtained by the total of its investment capital invested during such period in stocks, bonds and other securities (other than obligations of the United States and its instrumentalities and obligations of the state of New York, its political subdivisions and its instrumentalities); provided, however, that in case any investment capital is invested in any stock, bond or other security during only a portion of the period covered by the report, only such portion of such capital shall be taken into account; and provided further, that if a taxpayer's investment allocation percentage is zero, interest received on

bank accounts, on obligations of the United States and its instrumentalities and on obligations of the state of New York, its political subdivisions and its instrumentalities shall be multiplied by its business allocation percentage; provided, however, that with respect to corporations organized under article fifteen of the business corporation law, the investment allocation percentage shall be one hundred percent; and

(c) add the products so obtained.

(d) At the election of the taxpayer there shall be deducted from the portion of its entire net income allocated within the state either or both of the items set forth in subparagraphs one and two of this paragraph, except that only one of such deductions shall be allowed with respect to any one item of property.

New York Tax Law § 210(13)

13. (a) So long as the taxation procedures relating to a DISC provided in subparagraph (B) of paragraph (i) of subdivision nine of section two hundred eight of this article are in effect and not rendered invalid any taxpayer which during the taxable year being reported was a stockholder in any such DISC shall be allowed a DISC export credit, to be computed as hereinafter provided, against the tax imposed by this article after allowance of any credit permitted under subdivision eleven and subdivision twelve of this section. The amount of the credit shall be computed separately for each such DISC, based upon its operations during its annual reporting period ending the current taxable year of such stockholder, as follows:

(1) ascertaining the amount, if any, of such taxpayer's attributable share of the total current earnings and profits earned by such DISC for the reporting year which were included in its accumulated DISC income account pursuant to subsection (a) of section nine hundred ninety-six of the internal revenue code of nineteen hundred fifty-four,

(2) ascertaining a percentage by (i) totaling the gross receipts from the sale, lease, rental or other disposition of export property (as defined under subsection (c) of section nine hundred ninety-three of the internal revenue code of

nineteen hundred fifty-four) of the taxpayer by or to such DISC, and (ii) totaling such gross receipts from such export property of the taxpayer shipped from a regular place of business of the taxpayer within this state by or to such DISC and then (iii) dividing the total developed in (ii) above by that developed in (i) above (provided, however, for the purposes of this subparagraph, the tax commission may require such gross receipts to be computed on a similar basis for all such export property to properly reflect the percentage of such gross receipts attributable to export property shipped from a regular place of business of the taxpayer within this state),

(3) multiplying the amount ascertained in subparagraph one of this paragraph by the percentage ascertained in subparagraph two of this paragraph,

(4) ascertaining the amount of the taxpayer's taxable income as determined in subparagraphs one, two and three of this paragraph that is eligible for credit by multiplying the product ascertained in the preceding subparagraph by the taxpayer's business allocation percentage determined as provided in paragraph (a) of subdivision three of this section,

(5) the amount of DISC export credit attributable to the operations of each such DISC is then found by multiplying seventy percent of the taxpayer's taxable income that is eligible for credit, as computed in the preceding subparagraph, by the rate of tax applying to the taxpayer, as provided in subdivision one of this section,

(6) the taxpayer's total DISC export credit is the sum of the DISC export credits attributable to each DISC that qualifies for tax exemption under paragraph (i) of subdivision nine of section two hundred eight of this article, in which it was a stockholder during the taxable year being reported.

(b) The credit allowed under this subdivision for any taxable year shall not reduce the tax due for such year to less

than one hundred twenty-five dollars; nor may any unused credit be carried over to any following year.

New York Tax Law § 211(3)

1. Every taxpayer, as well as every foreign corporation having an officer, agent or representative within the state, shall annually on or before March fifteenth transmit to the tax commission a report in a form prescribed by it (except that a corporation which reports on the basis of a fiscal year shall transmit its report within two and one-half months after the close of its fiscal year and except, also, that a corporation which is a DISC shall transmit its report on or before the fifteenth day of the ninth month following the close of its calendar or fiscal year), setting forth such information as the tax commission may prescribe and every taxpayer which ceases to exercise its franchise or to be subject to the tax imposed by this article shall transmit to the tax commission a report on the date of such cessation or at such other time as the tax commission may require covering each year or period for which no report was theretofore filed. Every taxpayer shall also transmit such other reports and such facts and information as the tax commission may require in the administration of this article. The tax commission may grant a reasonable extension of time for filing reports whenever good cause exists.

An automatic extension of three months for the filing of its annual report shall be allowed any taxpayer if, within the time prescribed by the preceding paragraph, such taxpayer files with the tax commission an application for extension in such form as said commission may prescribe by regulation and pays on or before the date of such filing the amount properly estimated as its tax.

New York Tax Law § 211(4)

4. In the discretion of the tax commission, any taxpayer, which owns or controls either directly or indirectly substantially all the capital stock of one or more corporations, or substanially

all the capital stock of which is owned or controlled either directly or indirectly by one or more other corporations or by interests which own or control either directly or indirectly substantially all the capital stock of one or more other corporations, may be required or permitted to make a report on a combined basis covering any such other corporations and setting forth such information as the tax commission may require; provided, however, that any corporation which owns or controls either directly or indirectly substantially all the capital stock of a DISC not exempt from tax under paragraph (i) of subdivision nine of section two hundred eight of this article shall be allowed, at the election of such corporation, to make a report on a combined basis covering such DISC, but the failure of such corporation to make such election shall not prohibit the tax commission from requiring a combined report covering such corporation and such DISC; provided, further, that no combined report covering any corporation not a taxpayer shall be required unless the tax commission deems such a report necessary, because of inter-company transactions or some agreement understanding, arrangement or transaction referred to in subdivision five of this section, in order properly to reflect the tax liability under this article. In the case of a combined report the tax shall be measured by the combined entire net income or combined capital, of all the corporations included in the report. In computing combined entire net income intercorporate dividends shall be eliminated, in computing combined business and investment capital intercorporate stockholdings and intercorporate bills, notes and accounts receivable and payable and other intercorporate indebtedness shall be eliminated and in computing combined subsidiary capital intercorporate stockholdings shall be eliminated, provided, however, that intercorporate dividends from a DISC or a former DISC not exempt from tax under paragraph (i) of subdivision nine of section two hundred eight of this article which are taxable as business income under this article shall not be eliminated.

§ 211(5)

"5. In case it shall appear to the tax commission that any agreement, understanding or arrangement exists between the taxpayer and any other corporation or any person or firm, whereby the activity, business, income or capital of the taxpayer within the state is improperly or inaccurately reflected, the tax commission is authorized and empowered, in its discretion and in such manner as it may determine, to adjust items of income, deductions and capital, and to eliminate assets in computing any allocation percentage provided only that any income directly traceable thereto be also excluded from entire net income, so as equitably to determine the tax. Where (a) any taxpayer conducts its activity or business under any agreement, arrangement or understanding in such manner as either directly or indirectly to benefit its members or stockholders, or any of them, or any person or persons directly or indirectly interested in such activity or business, by entering into any transaction at more or less than a fair price which, but for such agreement, arrangement or understanding, might have been paid or received therefor, or (b) any taxpayer, a substantial portion of whose capital stock is owned either directly or indirectly by another corporation, enters into any transaction with such other corporation on such terms as to create an improper loss or net income, the tax commission may include in the entire net income of the taxpayer the fair profits which, but for such agreement, arrangement or understanding, the taxpayer might have derived from such transaction."

REGULATIONS OF THE NEW YORK STATE TAX COMMISSION (20 NEW YORK CODE OF RULES AND REGULATIONS)

DISC EXPORT CREDIT

Historical Note

Subpart (§§ 5-4.1—5-4.3) filed Aug. 31, 1976 eff. for all taxable years beginning on or after Jan. 1, 1976.

Section 5-4.1 General. [Tax Law, § 210(13)] Taxpayers that are stockholders of a tax exempt DISC are entitled to a DISC export credit if the export property, as defined in section 993 of the Internal Revenue Code, is shipped from the stockholder's regular place of business in New York State. A regular place of business is any bona fide office (other than a statutory office), factory, warehouse or other space which is regularly used by the taxpayer in carrying on its business.

Historical Note

Sec. filed Aug. 31, 1976; amd. filed April 1, 1981; eff. April 1, 1981.

5-4.2 Computation of the DISC export credit. [Tax Law, § 210(13)(a)] (a) The DISC export credit is computed as follows:

(1) Ascertain the taxpayer's attributable share of the total current earnings and profits earned by the DISC for the reporting period which is included in the accumulated DISC income account (see section 5-9.7 of this Title—Rules for treatment of earnings and profits).

(2) Ascertain a percentage by dividing the total of subparagraph (ii) by the total of subparagraph (i) of this paragraph.

(i) Determine the total gross receipts of the taxpayer from the sale, lease, rental or other disposition of its export property (not receipts from services or other types of property) by the DISC on behalf of the taxpayer, or from the sale, lease or rental of such property to the DISC.

(ii) Determine the total of the gross receipts described in subparagraph (i) of this paragraph, from the sale, lease, rental or other disposition of such export property which are shipped from a regular place of business of the taxpayer in New York State. For example, export property sold to the DISC and shipped by the taxpayer from its warehouse in New York State directly to the DISC's customers outside New York State or export property sold by the DISC as agent for the taxpayer and shipped by the taxpayer from its plant in New York State to the DISC outside New York State for subsequent shipment to the customer outside New York State.

(3) Multiply the amount ascertained in paragraph (1) of this subdivision by the percentage ascertained in paragraph (2) of this subdivision.

(4) Multiply the amount ascertained in paragraph (3) of this subdivision by the business allocation percentage computed on the stockholder's consolidated report for the taxable year.

(5) Multiply the amount ascertained in paragraph (4) of this subdivision by 70 percent.

(6) The amount determined in paragraph (5) of this subdivision is multiplied by the

5-4.3 Limitation and sequence of credits against tax. [Tax Law, § 210(13)]

(a) Credits against the tax allowable in this Subpart and this Part are applied in the following sequence:

(1) credit for eligible business facility (Subpart 5-1 of this Part);

(2) credit for sales or compensating use taxes on any catalytic, purifying or bleaching chemical agent (Subpart 5-5 of this Part);

(3) credit for sales or compensating use taxes on tangible personal property used in industrial waste treatment or pollution abatement (Subpart 5-6 of this Part);

(4) investment tax credit (Subpart 5-2 of this Part);

(5) employment incentive tax credit (Subpart 5-3 of this Part);

(6) DISC export credit (this Subpart); and

(7) the special additional mortgage recording tax credit (Subpart 5-7 of this Part).

(b) In no event may the tax due be less than the minimum tax described in section 3-5.1 of this Title. If after applying the investment tax credit and the employment incentive tax credit, the tax is the minimum tax, the DISC export credit is not allowed.

(c) There is no carry-over of the credits described in paragraph (1), (2), (3) or (6) of subdivision (a) of this section.